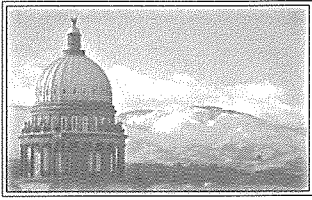


# State of Idaho Internal Control Report

Independent Auditor's Report on Internal Control over  
Financial Reporting and on Compliance and Other Matters  
Based on an Audit of Financial Statements  
Performed in Accordance with *Government Auditing Standards*

Fiscal Year 2008



# Legislative Services Office Idaho State Legislature

*Serving Idaho's Citizen Legislature*

**Jeff Youtz**  
Director

June 30, 2009

Honorable C.L. "Butch" Otter, Governor  
Honorable Members of the Legislature  
Honorable Donna M. Jones, State Controller

We are pleased to submit the State of Idaho *Internal Control Report* as it relates to our audit of the statewide *Comprehensive Annual Financial Report (CAFR)* covering the fiscal year ended June 30, 2008. This *Internal Control Report* is an integral part of the *CAFR* audit process and is required by *Government Auditing Standards* issued by the Comptroller General of the United States.

These standards require that we consider the internal control over financial reporting and disclose weaknesses that could have a material effect on the financial statements. We are also required to perform and disclose the results of tests of compliance with certain laws, regulations, and other requirements that could have a direct and material effect on the financial statement amounts.

The results of our audit identified seven weaknesses in internal control and no instances of noncompliance with certain laws, regulations, or other requirements. Although the risk of misstatement exists as a result of these issues, none of these weaknesses resulted in material misstatements that were not corrected as a result of the audit. As such, we were able to issue an unqualified opinion on the financial statements.

For your convenience, we have inserted the applicable portion of the agency's response after each issue and included the entire responses in Appendix A.

This report is available on our Web site at [www.legislature.idaho.gov](http://www.legislature.idaho.gov), and the *CAFR* can be obtained from the Idaho State Controller's Office on its Web site at [www.sco.idaho.gov](http://www.sco.idaho.gov) or by calling 208-334-3100.

Sincerely,



Don H. Berg, CGFM, Manager  
Legislative Audits Division

Mike Nugent, Manager  
Research & Legislation

Cathy Holland-Smith, Manager  
Budget & Policy Analysis

Don H. Berg, Manager  
Legislative Audits

Glenn Harris, Manager  
Information Technology

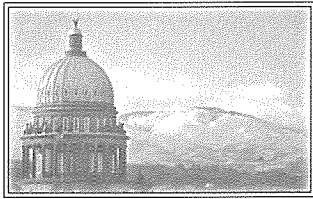
Statehouse, P.O. Box 83720  
Boise, Idaho 83720-0054

Tel: 208-334-2475  
[www.legislature.idaho.gov](http://www.legislature.idaho.gov)

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# Legislative Services Office Idaho State Legislature

*Serving Idaho's Citizen Legislature*

Jeff Youtz  
Director

December 23, 2008

**Independent Auditor's Report on Internal Control over Financial Reporting  
and on Compliance and Other Matters Based on an Audit of Financial Statements  
Performed in Accordance with *Government Auditing Standards***

Honorable C.L. "Butch" Otter, Governor  
Honorable Members of the Legislature  
Honorable Donna M. Jones, State Controller

We have audited the basic financial statements of the governmental activities, business-type activities, aggregate discretely presented component units, each major fund, and the aggregate remaining fund information for the State of Idaho, as of and for the fiscal year ended June 30, 2008, that collectively comprise the State's basic financial statements, and have issued our report thereon dated December 23, 2008. Our report was modified to include a reference to other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Other auditors audited the financial statements of the University of Idaho, Idaho State University, Boise State University, Lewis-Clark State College, Eastern Idaho Technical College and their respective component units, the Endowment Fund Investment Board, State Lottery Commission, Public Employees Retirement System of Idaho, IDEal Idaho College Savings Program, Idaho Life and Health Guaranty Association, Idaho Individual Risk Reinsurance Pool, Idaho Small Employer Health Reinsurance Program, Petroleum Clean Water Trust Fund, Idaho Building Authority, and Idaho Housing and Finance Association as described in our report on the State of Idaho's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting and compliance and other matters that are reported separately by those other auditors. The financial statements of the Idaho Life and Health Insurance Guaranty Association, Idaho Housing and Finance Association, and IDEal College Savings Program were not audited in accordance with *Government Auditing Standards*.

***Internal Control over Financial Reporting***

In planning and performing our audit, we considered the State of Idaho's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State of Idaho's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the State of Idaho's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

Mike Nugent, Manager  
Research & Legislation

Cathy Holland-Smith, Manager  
Budget & Policy Analysis

Don H. Berg, Manager  
Legislative Audits

Glenn Harris, Manager  
Information Technology

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the State of Idaho's financial statements that is more than inconsequential will not be prevented or detected by the State of Idaho's internal control. We consider all of the deficiencies described in the accompanying *Schedule of Findings and Responses* to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we do not consider any of the deficiencies described above to be material weaknesses.

#### ***Compliance and Other Matters***

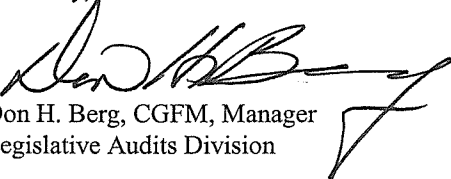
As part of obtaining reasonable assurance about whether the State of Idaho's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to the management of the State of Idaho in a separate correspondence issued at the State agency level.

Responses to the findings identified in our audit are described in the accompanying *Schedule of Findings and Responses*. We did not audit the responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of management of the State of Idaho, federal awarding agencies, and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

  
Don H. Berg, CGFM, Manager  
Legislative Audits Division

**STATE OF IDAHO  
INTERNAL CONTROL REPORT  
SCHEDULE OF FINDINGS AND RESPONSES  
FOR THE YEAR ENDED JUNE 30, 2008**

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**CONTROLLER, OFFICE OF THE STATE**

- 08S-1 Internal control weaknesses exist in the process for preparing the *Comprehensive Annual Financial Report (CAFR)*.
- 08S-2 The authority to originate and approve payroll transactions is not properly segregated.

**HEALTH AND WELFARE, DEPARTMENT OF**

- 08S-3 Estimates used to calculate Medicaid payables are not adjusted for changes in processes or fully documented.
- 08S-4 Monitoring and other control efforts over P-Cards are not consistently enforced.
- 08S-5 Over \$12,000 was paid for unallowable employee meals and refreshments.

**TREASURER, OFFICE OF THE STATE**

- 08S-6 Policies for selecting a contract investment management firm were not followed.
- 08S-7 A \$26.6 million variance exists between the Idle Pool Investment Account and individual agency cash balances that is not fully identified.

STATE OF IDAHO  
INTERNAL CONTROL REPORT  
FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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CONTROLLER, OFFICE OF THE STATE

**FINDING 08S-1**

Internal control weaknesses exist in the process for preparing the Comprehensive Annual Financial Report (CAFR). Internal controls are essential to ensure that financial statements are accurate and complete. We noted several control weaknesses that contributed to errors and omissions in the financial statements of the *CAFR*, which we are required by generally accepted auditing standards to disclose in the report. We noted the following conditions:

1. Revenue items and expenditure items were misclassified in the financial statements. For example, in the Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances, the remainder of the annual required contribution (ARC) for the other post-employment benefits (OPEB) liability in the amount of \$19.8 million was classified as a compensated absence instead of other long-term liability.
2. The Statement of Net Assets Invested in Capital Assets, Net of Related Debt was overstated by \$94.6 million for Governmental Activities and understated by \$11.5 million for Business-Type Activities.
3. Revenue and expenditures totaling \$57.4 million were overstated due to construction in progress activity at the Department of Administration.
4. Several prior period adjustments were made to the financial statements, which are indicators that internal control weaknesses exist.

Adjustments were made to the financial statements to correct the above conditions. The overall internal control structure of the State Controller's Office (SCO) is good, and these conditions represent isolated instances where controls should be reviewed and strengthened as appropriate.

**RECOMMENDATION**

**We recommend that the State Controller's Office review the internal controls over the preparation of the *CAFR* and strengthen the processes as appropriate. This review should include processes for ensuring the accuracy of the financial statements and note disclosures.**

**AGENCY'S CORRECTIVE  
ACTION PLAN**

1. Along with adding more review procedures, SCO will continue to work on internal controls and the new CAFR.net application that compiles the financial statements to make sure the appropriate funds, sub-objects, and structures are in place to ensure revenues and expenditures are classified correctly in all of the financial statements.
2. SCO has improved the instructions for reconciling the Invested in Capital Asset, Net of Related Debt, and has identified additional review steps to ensure the proper amounts are reported for the Statement of Net Assets Invested in Capital Assets, Net of Related Debt.

STATE OF IDAHO  
INTERNAL CONTROL REPORT  
FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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3. SCO will obtain the additional understanding and add additional review procedures to eliminate omissions and duplicate amounts reported by the Department of Public Works, Idaho State Building Authority, and agencies.
4. As SCO staff and agency staff gain expertise in financial reporting, they discover new information and perspectives about reporting requirements. While every effort will be made to capture all significant information that will make prior period adjustments unnecessary, SCO will continue to incorporate better reporting methods and data as that information comes to our attention.

**FINDING 08S-2**

The authority to originate and approve payroll transactions is not properly segregated. Payroll processing authority must be segregated so as not to create an opportunity for errors or irregularities to occur and go undetected. In general, the authority of approving transactions must not be given to employees who also have the authority to originate these transactions.

We identified 15 individuals at 13 agencies that have authority to originate and approve a new employee in the IPOPS system. In addition, eight of those individuals also have the authority in I-Time to create, approve, and submit time sheets. The Division of Statewide Payroll (EIS) has taken steps to significantly reduce the number of individuals that have authority to approve and originate in IPOPS. No new users have been set up with authority to perform both actions. The fact that there are still individuals with authority to originate and approve creates significant control weaknesses and increases the risk that errors or other irregularities could occur and not be detected.

**RECOMMENDATION**

**We recommend that the Division of Statewide Payroll require agencies to segregate the authority to originate and approve payroll transactions in the IPOPS and I-Time systems of those remaining individuals.**

**AGENCY'S CORRECTIVE  
ACTION PLAN**

EIS agrees with the statement that agencies need to segregate duties while originating and approving IPOPS transactions. In fact, EIS has provided a list of agencies/employees that have dual roles in IPOPS to the LSO CAFR auditor during the past six years and sent annual e-mail reminders and made phone calls to the individual agencies. Throughout this same six year period, EIS staff was instructed by the auditing team that we could not deny the agency's request for dual roles for existing employees, but could inform them of the risk they are taking and suggest adding another user to segregate the dual roles. Since 2003, we have not allowed users to be set up with dual role authority.

The number of agencies/employees who have had this role has shrunk significantly over the years. Agencies were reluctant to make this change due to the impact on their staffing. They would have to add more staff or additional duties to existing staff, especially the smaller agencies.

During our audit review in October, it was brought to our attention that we potentially could have a finding if we did not segregate the remaining individuals' duties in IPOPS and I-Time. As the management letter states, there were eight individuals who had dual roles in IPOPS and had authority in I-Time



STATE OF IDAHO  
INTERNAL CONTROL REPORT  
FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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to create, approve, and submit time sheets. On that same day, EIS staff called each one of these employees regarding these dual roles. Seven of the individuals immediately responded that same day that they would make the necessary arrangements to provide the proper segregation.

The last agency needed a few days to discuss internally the processing methods and then agreed to move forward with the segregation. It is ironic that the last agency to come into compliance was the auditors' agency, Legislative Services Office.

In conclusion, it is important to note that the EIS office has already fulfilled the recommendation. There are no more individuals who have authority to originate and approve personnel and payroll transactions in IPOPS and I-Time.

**HEALTH AND WELFARE, IDAHO DEPARTMENT OF**

**FINDING 08S-3**

Estimates used to calculate Medicaid payables are not adjusted for changes in processes or fully documented. Each year the Department is required to determine and report to the State Controller's Office the amount of Medicaid costs incurred but not yet paid as of June 30. These payable amounts have been based on estimates developed by the Department using a combination of current and prior year actual data and projected benefit costs and ratios.

The Department had not adjusted the estimates for calculating Medicaid payables for several years, even though significant changes have occurred that affect these calculations. In addition, adequate documentation was not available to determine the accuracy or basis for each estimate.

The Medicaid payment process has changed significantly over the past several years, where nearly all providers are now submitting billings and receiving payments electronically. In addition, there are fewer stale claims (those over 1 year old) than when this process was developed. Most claims are submitted and paid within 30 days from the date of service, frequently within seven days. Questioned claims represent less than 3% of the total claims.

Documentation of these estimates was incomplete or missing, which limits our ability to recalculate and confirm the accuracy of the amounts. We recalculated the amounts based on the existing data and known factors for the prior year and concluded that the amounts reported were reasonable. However, the lack of appropriate documentation and valid estimates raises the risk that amounts reported in future years could be materially misstated. The Department changed the process for 2008 to include actual claims received for 60 days after the year-end, for services provided prior to year-end. However, this was done only after we questioned the support for the prior process.

**RECOMMENDATION**

**We recommend that the Department review and document all estimates used to calculate the amount of Medicaid costs payable reported to the State Controller's Office.**

STATE OF IDAHO  
INTERNAL CONTROL REPORT  
FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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**AGENCY'S CORRECTIVE  
ACTION PLAN**

The Department agrees that all estimates should be reviewed later to make sure they are accurate and that all year-end estimates and calculations should be clearly documented. However, the Department disagrees that an estimate is necessary to determine Medicaid claims payable.

For fiscal year 2008, the year of this audit, the Department changed its method of calculating Medicaid payables to more closely follow State accounting policies. After the end of fiscal year 2008, the Department summed all Medicaid claims received 60 days after the end of the fiscal year for services rendered on or prior to June 30, 2008. According to the State's accounting policy, this sum equals Medicaid claims payable. This sum is not subject to estimation, so there is no need to verify accuracy of an estimate. This new method of calculation is not subject to variations and conditions described in the finding. It is a simple sum that is not subject to change.

The Department will clearly document the methodology and data for summing Medicaid claims paid after year-end. Additionally, the Department will review all year-end closing adjustments and make sure that any estimates are later verified for accuracy. However, Medicaid claims payable will not need to be verified because it is not an estimate.

**AUDITOR RESPONSE**

We appreciate the Department's response and agree that the State Controller's Office does provide guidance for reporting these payables. However, the guidance provided is not State accounting policy, but rather suggestions provided to assist the Department in gathering the information needed to report the payables. It is the Department's responsibility to ensure that the amount reported is accurate, complete, and substantiated.

Due to the complexity of Medicaid claims submission and processing, it is likely that a portion of these claims are not submitted until after the 60-day period currently used by the Department to estimate year-end Medicaid claims payable. This method does not take into consideration that providers have up to one year after the date of service to submit their claim. Some providers bill promptly and are paid within 30 days or less, while others are slow to submit their claims. The Department has no evidence that this risk was considered. We are also concerned that the Department still is not maintaining adequate documentation to confirm that the amounts reported include all material Medicaid claims payable as of June 30, 2008.

**FINDING 08S-4**

Monitoring and other control efforts over P-Cards are not consistently enforced. A high degree of control and monitoring is essential over P-Card usage, given the associated risks and the substantial volume of activity at the Department, exceeding \$6.6 million on nearly 40,000 transactions during fiscal year 2008. Although internal controls over the use of P-Cards have been developed and documented by the Department, some of these control efforts are not consistently monitored or enforced to limit the overall risks.

We noted that approvals are not performed by the appropriate staff, and sales taxes are paid on P-Card transactions in error.

**STATE OF IDAHO  
INTERNAL CONTROL REPORT  
FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

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Department policies require that a second-level approval be completed by the direct supervisor or manager of the P-Card user, and in no instance can the P-Card user be the second-level approver for their transactions. We tested a sample of transactions for 17 P-Cards assigned to administrative staff and determined that the second-level approver was consistently not a supervisor or manager for four of these P-Card users. In most cases, the second-level approver was the administrative assistant or other staff member who reports directly to the administrative staff member. We also randomly selected 65 transactions and identified four (6%) that were not approved by a direct supervisor as required.

Additionally, we noted a substantial number of P-Card transactions where sales tax was paid in error. State agencies are exempt from paying sales tax per Idaho Code, but nearly 25% of all P-Card users had one or more transactions where sales tax was paid. The most significant transactions involve payments for cell phone services where nearly two-thirds of all amounts had sales tax paid in error.

**RECOMMENDATION**

**We recommend that the Department strengthen monitoring and other control efforts over P-Card transactions by properly assigning second-level approvals for all users and notifying staff to avoid paying sales tax as specified by Idaho Code.**

**AGENCY'S CORRECTIVE  
ACTION PLAN**

The Department agrees that some second level P-Card approvals during the testing period (July 1, 2007 – June 30, 2008) were not performed by a direct supervisor or, in the case of managerial staff, were performed by staff members who reported to the cardholder. To clarify, the Department enacted the policy to which the auditor refers on May 28, 2008, and full implementation will not be completed until August 2009, so it would anticipate some exceptions during the testing period. The Department disagrees with the auditor's conclusions about the sales taxes paid by the Department during the testing period, particularly the assertion that two-thirds of all payments for cell phone services had sales taxes paid in error.

Since May, the P-Card administrator has been changing the approver structure for the Department's over 650 cardholders. The structure change will ensure that the second level approver assigned for every cardholder is "a designated supervisor or manager in the cardholder's divisional line of authority...with direct knowledge of the cardholder's assigned work activities," as required by policy.

Each Division needs to determine the appropriate staff member to act as second level approver, and the approvers will need to receive training. The Department anticipates full implementation by August 2009.

As an added control over the P-Cards of high-level managerial staff, by April 30, 2009 the Department will create a separate approval group for cardholders who are division administrators and above. The executive assistant to the director will be assigned as the level two approver for this group.

**STATE OF IDAHO  
INTERNAL CONTROL REPORT  
FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

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There are several problems with the data the auditor used to conclude the Department was paying sales tax unnecessarily on P-Card transactions.

- Several of the transactions took place outside of Idaho. As an agency of the State of Idaho, the Department is not exempt from sales tax in other states, therefore these are appropriate charges.
- A quirk in the P-Card download report causes it to duplicate the amount of taxes paid whenever a transaction is split between multiple PCAs in the P-Card system. If the true amount of taxes paid is then refunded, it still looks like the Department has paid tax when it has not because of the error in this report.
- The cell phone services the auditor mentions are Verizon Wireless. In the P-Card download report, the "Taxes, Governmental Surcharges and Fees" listed on the Verizon bills come across in the tax column. Examination of the actual bills, however, reveals that these charges are various fees (Federal Universal Service Charge, Regulatory Charge, Ada County 911 Fee). None is Idaho state sales tax, thus the Department is not exempt from paying them and the charges are legitimate.

After accounting for the issues mentioned in the above paragraph, we estimate that out of the \$6,621,243 the Department paid through the P-Card system in fiscal year 2008, there were 265 transactions where sales tax was paid and not refunded, for a total of \$1,738.37 sales tax paid. This equates to 0.7% of the P-Card transactions being paid with sales tax, and the sales tax paid equals 0.03% of the total P-Card dollar volume. We were unable to examine every transaction reported as taxed in the time allowed for this response, so the above estimate may overstate the sales tax the Department actually paid.

The Department will continue to make every effort to avoid paying sales tax, reminding staff that Departmental transactions are exempt from sales tax under Idaho Code and, when practicable, requesting refunds when a vendor mistakenly charges sales tax.

The Department will additionally study the cost effectiveness of implementing: 1) a periodic review of all P-Card transaction data to determine particular cardholders who may need more training on the Department's tax-exempt status; and 2) a monthly submission of form TCR to the State Tax Commission to recoup any sales tax erroneously paid and not refunded.

**AUDITOR RESPONSE**

We appreciate the Department's response and will continue to monitor progress to resolve this issue.

The policy change on second level approvers was effective in May 2008, but we are concerned that implementation will take 15 months (August 2009) to complete. We are also concerned that the Department identified "a quirk" in the P-Card download report as the cause for possible sales tax expenses that should not have been paid at all, but no remedy or correction action is identified.

**STATE OF IDAHO  
INTERNAL CONTROL REPORT  
FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

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**FINDING 08S-5**

Over \$12,000 was paid for unallowable employee meals and refreshments. State travel policies prohibit the use of State funds for meals and refreshments at regularly scheduled staff meetings or department-sponsored social gatherings, unless the meeting occurs not more than quarterly and attendees are brought from various locations throughout the State. The Department also has specific employee recognition event policies that are more restrictive than the general State travel policies.

In May 2008, the Governor proclaimed May 5 through 9 as "Public Employee Recognition Week," with May 7 designated as "State Employee Recognition Day." During this week, we identified 80 transactions totaling more than \$12,000 for various meals and refreshments, including pizza parties, lunches, and snacks for several days that week for 100 staff. Most transactions did not have any supporting documentation, such as an agenda or attendee list, to determine whether the costs were allowable under State travel policies.

**RECOMMENDATION**

**We recommend that the Department comply with State travel policies and Department employee recognition event policies and monitor meal and refreshment costs to ensure that amounts are appropriate and allowable. We further recommend that any future expenditures of this nature be submitted to the State Board of Examiners for approval prior to payment.**

**AGENCY'S CORRECTIVE  
ACTION PLAN**

The Department disagrees with the auditor's conclusion that the \$12,000 paid was for "unallowable employee meals and refreshments." It is true that there is no specific guidance regarding activities during Public Employee Recognition Week. However, the State travel policy, as cited by the auditor, refers to sponsored meeting and training sessions. Public Employee Recognition Week, as declared by the Governor, is completely separate and a completely different matter. There is no mention in the State travel policy, nor in any other of the Board of Examiner's regulations, regarding employee recognition events; therefore, it is inaccurate to say the costs are unallowable per State travel policy.

The finding additionally claims the Department spent "more than \$12,000 for various meals and refreshments, including pizza parties, lunches and snacks for several days that week for 100 staff." As the auditor's documentation shows, this is incorrect. The Department spent slightly more than \$12,000; this was for over 3,200 employees, an average of roughly \$3.75 per employee.

Given the lack of guidance regarding Public Employee Recognition Week events, should the Department decide to hold such events in future years, it will seek the approval of the Board of Examiners.

**AUDITOR RESPONSE**

The existing Board of Examiner's travel policies provide limits and methods for determining allowable meal and refreshment costs. Given that the declaration by the Governor did not identify or authorize expenditures for particular activities, the Department is bound by the limits established in the Board of Examiner's travel policies as they relate to meal and refreshments for employees.

STATE OF IDAHO  
INTERNAL CONTROL REPORT  
FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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The primary example of questionable meal costs related to one division within the Department that has a total of 106 staff. During the Public Employee Recognition Week, this division incurred \$1,537 to provide two lunches and one breakfast for approximately 100 staff. Travel policies prohibit meal costs for regularly scheduled staff meetings or department-sponsored social gatherings, unless such meetings occur no more than quarterly and attendees are brought together from various locations throughout the State. These meal costs do not qualify under this provision as all employees of the division are located in Boise and meals were provided on multiple days. Similar costs were incurred by other divisions and units of the Department.

**TREASURER, OFFICE OF THE STATE**

**FINDING 08S-6**

The process for selecting a contract investment management firm was not documented. The State Treasurer's Office has developed sound written policies for evaluating and selecting investment instruments and investment management firms. These policies have been in place for several years and also require an annual review by an independent auditor to ensure compliance and to address any internal control issues.

During our annual review of the Treasurer's office policies, we identified one contract with an investment management firm in which the State Treasurer's Office did not maintain documentation to support the selection of the firm. This contract was with a firm to manage \$50 million of the approximately \$1.6 billion Local Government Investment Pool at an estimated annual cost of \$70,000 using a 14 basis point fee calculation.

The State Treasurer's Office is not required statutorily to use a formal process to select vendors, but sound internal control practices and the Treasurer's own established policies should be followed to ensure that the most favorable terms, conditions, and price for services are attained and documented. This particular investment management firm also did not report activities as required by the Treasurer's policies, which has limited the Treasurer's ability to gauge the firm's performance.

**RECOMMENDATION**

**We recommend that the State Treasurer's Office retain documentation that shows that the selection process resulted in the Office receiving the most favorable terms, conditions, and price for services. We also recommend that the State Treasurer's Office reevaluate the investment management contract in question to determine whether or not to continue, amend, or cancel this contract.**

**AGENCY'S CORRECTIVE  
ACTION PLAN**

The State Treasurer's Office agrees with the audit finding and will retain adequate documentation of all subsequent selection processes. The Treasurer's Office has always taken great care in the selection process when managing State funds, and this particular contract selection was no different, in that we pursued our normal due diligence in analyzing the most favorable terms, conditions, and price in the selection of the firm. However, documentation of this process should have been more complete and will be in the future. We also determined that the management firm selected did not follow up with adequate reporting consistent with our policies, so we terminated the contract earlier this year.

**STATE OF IDAHO  
INTERNAL CONTROL REPORT  
FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

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**FINDING 08S-7**

A \$26.6 million variance exists between the Idle Pool Investment Account and individual agency cash balances that is not fully identified. The Office's internal accounting records for the Idle Pool Investment Account do not agree with the bank statement of holdings. This variance has not been specifically identified or properly accounted for by the State Treasurer's Office.

This variance is attributable to several factors, including the method of earnings distribution. Earnings are distributed monthly in accordance with generally accepted accounting principles based on an accrual calculation that includes the recognition of accretion and amortizations before the actual cash is received and deposited. This creates a variance between the total agency cash balances and the cash balance recorded in the Pool.

Although the monthly variance is tracked, the specific details are not identified and the State Treasurer's Office has determined that at least \$200,000 of the \$26.6 million variance at June 2008 is not related to the change in accounting method. This raises the possibility that errors exist that are not be identified and corrected.

At year end, the State Treasurer's Office records an unsupported transaction to the Pool equal to the difference needed to reconcile the accounts. This adjustment is reversed at the beginning of the next year. The entry of unsupported transactions into the accounting system illustrates a lack of proper internal controls.

**RECOMMENDATION**

**We recommend that the State Treasurer's Office perform additional analysis to identify the details of the variance between the individual agency cash balances and the actual cash balance in the Idle Pool Investment Account. We also recommend that the State Treasurer's Office implement internal controls to ensure that all transactions recorded to the Pool are properly initiated, supported, and reviewed.**

**AGENCY'S CORRECTIVE  
ACTION PLAN**

The \$26.6 million variance has been identified and a monthly reconciliation has been implemented.

In response to the Treasurer's Office recording an unsupported transaction to the Pool, this is a separate issue from the \$26.6 million. Our current system is not able to store the difference between transfers in and transfers out when we close out a fiscal year. To carryover the difference, we create an entry which always nets to zero, with one half of the transaction done on the last day of the fiscal year, and the other done on the first day of the fiscal year. The Treasurer's Office has plans to update its banking software within the next few years and will address the issue at that time.

# APPENDIX A

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Responses from agencies to the findings and recommendations of this report.





STATE OF IDAHO  
OFFICE OF THE STATE CONTROLLER  
DONNA M. JONES

February 20, 2009

Mr. Don H. Berg, CGFM, Manager  
Legislative Audits Division  
954 West Jefferson Street, Second Floor  
Boise, ID 83702

Dear Mr. Berg:

Thank you for the opportunity to respond to the findings in the audit of the State's Comprehensive Annual Financial Report (CAFR).

*Finding #1 – Internal control weaknesses exist in the process for preparing the Comprehensive Annual Financial Report (CAFR).*

1. Revenue items and expenditure items were misclassified in the financial statements.

*SCO Response:*

Along with adding more review procedures, SCO will continue to work on internal controls and the new CAFR.net application that compiles the financial statements to make sure the appropriate funds, subobjects, and structures are in place to ensure revenues and expenditures are classified correctly in all of the financial statements.

2. The Statement of Net Assets Invested in Capital Assets, Net of Related Debt was overstated by \$94.6 million for Governmental Activities and understated by \$11.5 million for Business-Type Activities.

*SCO Response:*

SCO has improved the instructions for reconciling the Invested in Capital Asset, Net of Related Debt, and has identified additional review steps to ensure the proper amounts are reported for Statement of Net Assets Invested in Capital Assets, Net of Related Debt.

3. Revenue and expenditures totaling \$57.4 million were overstated due to construction in progress activity at the Department of Administration.

*SCO Response:*

SCO will obtain the additional understanding and add additional review procedures to eliminate omissions and duplicate amounts reported by the Department of Public Works, Idaho State Building Authority, and agencies.

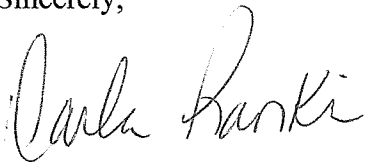
4. Several prior period adjustments were made to the financial statements, which are indicators that internal control weaknesses exist.

*SCO Response:*

As SCO staff and agency staff gain expertise in financial reporting, they discover new information and perspectives about reporting requirements. While every effort will be made to capture all significant information that will make prior period adjustments unnecessary, SCO will continue to incorporate better reporting methods and data as that information comes to our attention.

We appreciate your staff's professionalism, very thorough audit of the State's financial statements, and their hard work to complete the CAFR by the statutory deadline. Thank you for your helpful comments.

Sincerely,



Darla K. Rankin  
Deputy State Controller



STATE OF IDAHO  
OFFICE OF THE STATE CONTROLLER  
DONNA M. JONES

February 19, 2009

Don H. Berg, Manager  
Legislative Audits Division  
Statehouse Mail

Dear Mr. Berg:

Thank you for the opportunity to respond and comment on the February, 6, 2009, Management Letter report. It has been a pleasure to work with you and your staff throughout this process.

Our office agrees with the statement that agencies need to have segregated duties while originating and approving IPOPS transactions. In fact our office has partnered with your LSO auditor teams over the past several years on this very item. Our staff has provided a list of agencies/employees that have dual roles in IPOPS to the LSO CAFR auditor during the past six years and sent annual e-mail reminders and made phone calls to the individual agencies. Throughout this same six year period, our staff was instructed by the auditing team that we could not deny the agency's request for dual roles for existing employees, but we could inform them of the risk they are taking and suggest adding another user to segregate the dual roles. Since 2003, we have not allowed new users to be set up with dual role authority.

The number of agencies/employees who have had this role has shrunk significantly over the years. Agencies were reluctant to make this change due to the impact on their staffing. They would have to add more staff or add additional duties to existing staff, especially the smaller agencies.

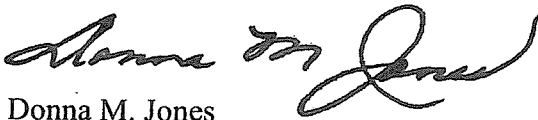
During our audit review in October, it was brought to our attention that we potential could have a finding if we did not segregate the remaining individuals' duties in IPOPS and I-Time. As the management letter states, there were eight individuals who had dual roles in IPOPS and had authority in I-Time to create, approve, and submit time sheets. On that same day, our staff called each one of these employees regarding these dual roles. Seven of the individuals immediately responded that same day that they would make the necessary arrangements to provide the proper segregation.

The last agency needed a few days to discuss internally the processing methods and then agreed to move forward with the segregation. It is ironic that the last agency to come into compliance was your own agency, Legislative Services Office.

In conclusion, it is important to note that our office has already fulfilled your recommendation. There are no more individuals who have authority to originate and approve personnel and payroll transactions in IPOPS and I-Time.

Once again, our office appreciates your team's recommendations to make our state's financial systems more secure and sound. We too appreciate the cooperation and assistance they provided to us during this review.

Sincerely,

A handwritten signature in cursive script, appearing to read "Donna M. Jones".

Donna M. Jones

Cc: Jeff Youtz



IDAHO DEPARTMENT OF  
HEALTH & WELFARE

C.L. "BUTCH" OTTER - GOVERNOR  
RICHARD M. ARMSTRONG - DIRECTOR

OFFICE OF THE DIRECTOR  
450 W. State Street, 10th Floor  
P.O. Box 83720  
Boise, ID 83720-0036  
PHONE 208-334-5500  
FAX 208-334-6558

March 31, 2009

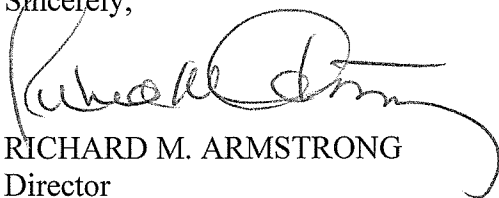
Don Berg, Manager  
Legislative Audits Division  
Legislative Services Office  
P.O. Box 83720  
Boise, Idaho 83720-0054

Dear Mr. Berg:

The Department of Health and Welfare has reviewed and responded to the recommendations presented in the Comprehensive Annual Financial Report for Fiscal Year 2008. Enclosed is a copy of our reply to each item addressed in the audit.

Thank you for the opportunity to respond to the findings.

Sincerely,



RICHARD M. ARMSTRONG  
Director

RMA/eb

enclosure

RON G. CRANE  
STATE TREASURER



(208) 334-3200  
(208) 332-2960 FAX

**STATE OF IDAHO  
OFFICE OF THE STATE TREASURER**

ROOM 102 STATEHOUSE  
P.O. BOX 83720  
BOISE, IDAHO 83720-0091

April Renfro  
Legislative Audits  
954 W. Jefferson St. 2<sup>nd</sup> Floor  
Boise, ID 83720-0054

July 20, 2009

Dear Ms. Renfro:

Thank you for the results of the State Treasurer's Office audit in regard to the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2008. I have reviewed the legislative audit and accept it as presented.

As always it is a pleasure to work with you and your staff. I appreciate your efforts to streamline and improve the operations of our office.

Sincerely,

A handwritten signature in black ink, appearing to read "Ron G. Crane". The signature is fluid and cursive, with the first name "Ron" and last name "Crane" clearly distinguishable.

Ron G. Crane  
State Treasurer

RON G. CRANE  
STATE TREASURER



(208) 334-3200  
(208) 322-2960 FAX

STATE OF IDAHO  
OFFICE OF THE STATE TREASURER

P.O. Box 83720  
BOISE, IDAHO 83720-0091

April Renfro  
Legislative Audits  
954 W. Jefferson St. 2<sup>nd</sup> Floor  
Boise, ID 83720-0054

July 23, 2009

Dear Ms. Renfro:

In reply to the FY 2008 legislative audit in regard to the Comprehensive Annual Financial Report (CAFR), the Treasurer's Office responds as follows:

Finding #1 – The process for selecting a contract investment management firm was not documented.

We agree with the audit finding and will retain adequate documentation of all subsequent selection processes. The Treasurer's Office has always taken great care in the selection process when managing state funds, and this particular contract selection was no different, in that we pursued our normal due diligence in analyzing the most favorable terms, conditions, and price in the selection of the firm. However, documentation of this process should have been more complete and will be in the future. We also determined that the management firm selected did not follow up with adequate reporting consistent with our policies, so we terminated the contract earlier this year.

Finding #2 – A \$26.6 million variance exists between the Idle Pool Investment Account and individual agency cash balances that are not fully identified.

The \$26.6 million variance has been identified and a monthly reconciliation has been implemented.

In response to the STO recording an unsupported transaction to the Pool, this is a separate issue from the \$26.6 million. Our current system is not able to store the difference between transfers in and transfers out when we close out a fiscal year. To carry over the difference we create an entry which always nets to zero with one half of the transaction done on the last day of the fiscal year, and the other done on the first day of the fiscal year. The STO has plans to update our banking software within the next few years and will address the issue at that time.

Sincerely,

A handwritten signature in cursive script, appearing to read "Ron G. Crane".

Ron G. Crane  
State Treasurer